Issue Date	September 29, 2004
Audit Case Number	2004-DE-1004

TO: John C. Weicher, Assistant Secretary for Housing-Federal Housing Commissioner, H

FROM: Robert C. Gwin, Regional Inspector General for Audit, Denver Region, 8AGA

SUBJECT: New Freedom, Salt Lake City, UT, Did Not Fully Disclose the Intended Use of Payments Collected from Borrowers of Streamline-refinanced Loans

HIGHLIGHTS

What We Audited and Why

We audited New Freedom Mortgage Corporation (New Freedom), in Salt Lake City, UT. We selected New Freedom for review because it is a large nationwide mortgagee with the origination and refinancing of Federal Housing Administration insured loans as its main source of revenue. After the audit was initiated, we were notified by Denver Homeownership Center program personnel that they were in contact with New Freedom and its lawyers concerning some of New Freedom's business operating practices. Based on conversations with Denver program personnel, we decided to concentrate our review on New Freedom's streamline refinancing of insured loans. During our audit period, New Freedom originated 32,967 Federal Housing Administration-insured loans nationwide, with a total original mortgage amount of $3,164,265,358. Of those loans, 21,721 were streamline-refinanced loans valued at $1,892,984,443.

Our audit objectives were to determine (1) whether New Freedom complied with Real Estate Settlement Procedures Act (the Act) and U. S. Department of Housing and Urban Development (HUD) related requirements when streamline refinancing

Federal Housing Administration insured loans and (2) whether New Freedom's Quality Control Plan, as implemented, meets HUD requirements.

What We Found

New Freedom did not comply with the Act and HUD related requirements in the streamline refinancing of Federal Housing Administration insured loans. New Freedom collected an inappropriate monthly mortgage payment from borrowers of streamline-refinanced loans. New Freedom collected these payments to help offset its lender-paid closing costs on its advertised "no closing cost to you" streamline-refinanced loans. Because borrowers believed these payments to be the last mortgage payment on their existing loans and because New Freedom did not fully disclose all costs associated with the streamline-refinanced loans, borrowers were unable to make informed decisions concerning their refinanced loans. Our testing showed that from a sample of 866 loans reviewed, New Freedom collected $156,998 in inappropriate monthly mortgage payments on 598 of those loans.

New Freedom's quality control program was in compliance with HUD requirements and it own written policies and procedures. The program also ensured that deficiencies were identified and corrected in a timely manner.

What We Recommend

We recommend that you require New Freedom to reimburse the borrowers or HUD for the inappropriate monthly mortgage payments collected on the insured streamline refinanced loans. In addition, you should refer New Freedom to the Office of RESPA and Interstate Land Sales for review. For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06 REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided a discussion draft of our audit report to New Freedom on August 26, 2004, and requested their comments by September 10, 2004. Per New Freedom's request, we agreed to extend the due date for their comments to September 20, 2004. We received New Freedom's written response by the agreed upon date of September 20, 2004. New Freedom generally disagreed with the finding, as they believed the situation to be a matter of misunderstanding. The complete text of the New Freedom's response, along with our evaluation of that response, can be found in Appendix B of this report.

TABLE OF CONTENTS

BACKGROUND AND OBJECTIVES

New Freedom Mortgage Corporation (New Freedom) was established on December 28, 1995, in the State of Utah as a domestic corporation. It was approved by the U. S. Department of Housing and Urban Development (HUD) to originate and underwrite Federal Housing Administration-insured loans, under HUD's Title II Single Family Direct Endorsement Program, as a non-supervised direct endorser on June 20, 1996. New Freedom's main office is located in Salt Lake City, UT. At the time of our review, New Freedom had 17 active branch offices.

New Freedom's principal activity is the origination and underwriting of mortgages under the HUD Single Family Direct Endorsement Program. New Freedom underwrites the loans it originates and is required to supervise and perform quality control reviews of its operations. New Freedom rarely services the loans it originates and underwrites but sells them almost immediately to its investors.

During our audit period, March 1, 2002, through February 29, 2004, the majority of New Freedom's business was streamline refinancing of Federal Housing Administration-insured loans. Over this period, its streamline refinancing business increased dramatically. Approximately 75 percent of its portfolio was Federal Housing Administration-insured loans and approximately 75 percent of those loans were streamline-refinanced loans. During our audit period, New Freedom originated 32,967 Federal Housing Administration-insured loans nationwide. Of those, 21,721 were streamline-refinanced loans.

Initially we focused our review on Federal Housing Administration-insured loans refinanced in the State of Utah. New Freedom originated 2,663 Federal Housing Administration-insured loans in Utah between March 1, 2002, and February 29, 2004. Of those, 1,661 were streamline-refinanced loans, 66 of which defaulted. The total mortgage amount for the 2,663 Federal Housing Administration-insured loans was $330,475,943. Of those loans, 1,906 are active, 18 are in claim status, and 739 have been terminated. The total of all claims paid for the 18 loans in claim status was $1,724,900.

Since a large majority of New Freedom's business was Federal Housing Administration-insured streamline-refinanced loans, we focused our review on streamline-refinanced loans. Our audit objectives were to determine (1) whether New Freedom complied with the Act and HUD related requirements when streamline refinancing Federal Housing Administration insured loans and (2) whether New Freedom's Quality Control Plan, as implemented, meets HUD requirements.

RESULTS OF AUDIT

Finding: New Freedom Did Not Fully Disclose the Intended Use of the Prior Loan's Monthly Mortgage Payment Collected from Borrowers of Streamline-Refinanced Loans.

New Freedom collected an inappropriate monthly mortgage payment from borrowers of streamline-refinanced Federal Housing Administration-insured loans; contrary to both the Act and HUD related requirements (see Appendix C). New Freedom was collecting this money to help offset its own lender-paid closing costs on its advertised "no closing cost to you" streamline-refinanced loans. Because borrowers believed these payments were the last mortgage payment on their existing loans and New Freedom did not fully disclose all costs associated with the streamline-refinanced loans, borrowers were not afforded the opportunity to make an informed decision concerning their refinanced loans.

Testing showed that approximately 70.22 percent of all streamline-refinanced federally insured loans, processed out of the Salt Lake City, UT office, charged borrowers the inappropriate monthly mortgage payment. Eight hundred and sixty six streamline-refinanced insured loans were tested during our audit and 598 of those loans were charged the inappropriate monthly mortgage payments. Our testing also showed that the average amount of overcharged money collected, on those loans, was approximately $262, for a total of $156,998 in inappropriate monthly mortgage payments. While New Freedom has stopped the practice of collecting the inappropriate monthly mortgage payment, approximately 15,252 borrowers of the federally insured streamline-refinanced loans may have paid this inappropriate payment.

Inappropriate Collection of Borrowers' Monthly Mortgage Payment on Prior Loan

New Freedom inappropriately collected an additional monthly mortgage payment on prior loans from its borrowers of federally insured streamline-refinanced loans. All of these loans were streamline-refinanced loans without appraisals. According to New Freedom's own research, it charged the borrower an additional monthly mortgage payment on a prior loan in approximately 70.22 percent of a sample 796 streamline-refinanced loan cases. In these cases, the HUD-1 Settlement Statement identifies the payment collected as the next month's mortgage payment. For example, if a loan closed toward the end of January, the HUD-1 Settlement Statement would show a February mortgage payment.

The HUD-1 Settlement Statement is a standard form that should clearly show all charges imposed on the borrowers in connection with the settlement. The HUD-1 Settlement Statement is supposed to show the actual settlement costs of the loan transaction. The mortgage company must clearly disclose all fees charged in settlement transactions so that the consumer (i.e. borrower) can understand the nature and recipient of the payments. New Freedom did not clearly disclose the true nature of the collected monthly mortgage payment to the borrowers.

Generally, New Freedom required the borrower to bring to closing one monthly mortgage payment, which usually included principal, interest, taxes, and insurance. This situation would occur whenever HUD's streamline refinance requirements did not allow the borrower to roll the interest that was due to the prior servicer, on the old loan, into the new loan. New Freedom would have the borrower make out a post dated check, payable to New Freedom, for the entire mortgage payment amount on the prior loan. New Freedom is entitled to the last month's interest since it is required to pay this amount to the prior servicer. However, it is not entitled to obtain and keep the prior loan's principal, taxes, and insurance without applying these amounts to the old loan.

Eight hundred and sixty six Federal Housing Administration-insured loans were tested during our review. The Office of Inspector General (OIG) auditors reviewed 70 loans and New Freedom's Quality Control Division reviewed 796 loans. Five hundred and ninety eight of those loans were charged the inappropriate monthly mortgage payments. New Freedom overcharged the borrowers of the 598 loans approximately $156,998 for inappropriate principal, taxes, and insurance.

During our detailed analysis of 16 federally insured streamline-refinanced loans, we identified that six of those loans contained the inappropriate monthly mortgage payment. The inappropriate principal, taxes, and insurance collected ranged from $152 to $341. We also interviewed six borrowers in the Denver Metropolitan area who were also charged the inappropriately monthly mortgage payment. The inappropriate principal, taxes, and insurance collected ranged from $185 to $455.

New Freedom performed testing of 796 of the streamline-refinanced loans refinanced out of its Salt Lake City, UT office and determined that 559 of those loans had the inappropriate monthly mortgage payment. This means that 70.22 percent of the streamline-refinanced loans tested contained the inappropriate monthly mortgage payment. New Freedom did not perform an analysis to determine the average amount of the inappropriate payments. We analyzed New Freedom's testing and verified that it was supported. We selected one of the same months New Freedom reviewed and we choose a separate sample of 48 loans to analyze. Of those loans, 27 loans had the inappropriate monthly mortgage payment. The results of our review were comparable with the results of New Freedom's review.

We computed the average amount of the inappropriate principal, taxes, and insurance collected for the 39 loans reviewed by the OIG was $262. Applying this average to the 598 loans reviewed, we determined that New Freedom overcharged the borrowers approximately $156,998.

New Freedom streamline-refinanced 21,721 Federal Housing Administration-insured loans from March 1, 2002, through February 29, 2004. Taking 70.22% of the 21,721 loans refinanced, we estimated that 15,252 loans were charged the inappropriate monthly mortgage payment. We multiplied the 15,252 loans times the average inappropriate payment of $262. This computation equals $3,996,024 in inappropriate principal, taxes, and insurance that was collected from the borrowers during our audit period.

According to New Freedom officials, the collection of the principal, taxes, and insurance via a post dated check was not an attempt to mislead the borrowers but, rather a way to offset the lender-paid closing costs, while providing borrowers with time to obtain the funds needed to close the loan. New Freedom officials stated that one of the reasons they have borrowers write a post dated check to New Freedom, rather than bring the funds to closing, is that some States have a "good funds" law. This means that the title company will not accept a personal check, and the borrower must provide certified funds at closing. When the borrower writes the check to New Freedom, the check is post-dated for the 15th of the next month, allowing the borrower time to obtain the money and perhaps get money back from the prior escrow account. Therefore, New Freedom officials believed that its practice of collecting the final payment on the prior loan was to the borrower's advantage, by helping them to streamline refinance their old loan without having to pay any out-of-pocket costs at closing. Further, New Freedom officials contented that they disclosed to the borrowers what the payment was applied toward, and the borrowers should have been aware of how New Freedom applied the payment.

New Freedom Did Not Accurately Disclose How the Monthly Mortgage Payment Was Applied

We found that New Freedom did not disclose to its borrowers how the monthly mortgage payment would be used. New Freedom advertised "no closing cost to you" streamline refinancing of Federal Housing Administration-insured loans on a mass-mailed flyer. The flyer also stated, "You may have to make one last payment on your present loan and/or possibly repay New Freedom for escrows advanced or escrow shortages on your current loan." Additionally, New Freedom sends out a package of documents to borrowers to inform them about the streamline refinancing process. Included in this package is a copy of the "Good Faith Estimate." In the cases we reviewed, that had the inappropriate monthly mortgage payment, the good faith estimate did not disclose this payment as a charge to the borrower even though New Freedom was aware that the borrower would most likely incur this charge.

Also included in the package was a document, entitled "Streamline Questions and Answers," that contains the following question and answer:

> ***"Q - Do I have to bring any funds to closing? A – Yes.*** *At closing you will bring in the last payment on your old loan, unless you qualify to roll in the final payment into your new Streamline FHA Refinance. You may post-date your final payment to the 15th of the following month, which will pay off your current loan."*

Borrowers may owe interest to the prior mortgagee on the unpaid principal balance from the date the last payment was made until the date the loan is paid off, but, in most cases, they do not owe the principal, taxes, and insurance, to the prior mortgagee. New Freedom should only charge the borrower for costs incurred and due to the prior servicer on the old loan. New Freedom did not apply the money collected for principal, taxes, and insurance from the inappropriate monthly mortgage payment to the prior loan. The way New Freedom disclosed the monthly mortgage payment to the borrower, the principal collected should reduce the principal amount of the prior loan, and the taxes and insurance should be applied to their prior escrow account. Since the principal collected was not applied to the prior mortgage, New Freedom should reduce the principal amount of the new loan. Likewise, since the taxes and insurance collected were not applied to the old escrow account, they should be applied to the new escrow account. Instead, New Freedom used the money to pay some of the closing costs incurred in the loan transaction.

Borrowers were not aware, and the disclosure documents did not indicate, that a portion of the monthly mortgage payment was not applied to their prior loan, but was used to pay closing costs. We interviewed six borrowers who were charged the inappropriate monthly mortgage payment to determine their understanding of what the monthly mortgage payment was for. All six of the borrowers believed that the monthly mortgage payment they were required to pay at closing was for their prior loan. The borrowers stated that their understanding was that New Freedom paid their last month's payment for them and that they were merely paying New Freedom back. We verified that all six of the borrowers had received the "Streamline Questions and Answers" and/or the "Supplementary Closing Instructions for Our Borrower" documents. The "Streamline Questions and Answers" document stated that collecting the last month's mortgage payment "will pay off your current loan." The "Supplementary Closing Instructions for Our Borrower" document, which was initialed by the borrower, outlined what items the borrower was required to bring to closing. It states that the purpose of the post-dated check was for "Final Payment on Current Loan." This type of business practice is in violation of the Act and HUD's related requirements concerning disclosure.

New Freedom Recognized the Situation and Revised Its Policies and Procedures

Because of discussions between New Freedom officials and the Denver Homeownership program personnel, New Freedom officials were aware of the confusion with its practice of collecting the final monthly payment on the old loan. As of May 2004, New Freedom revised its policies and procedures for calculating the closing costs required of the borrower. It has also changed the way it discloses on the HUD-1 Settlement Statement the fees and charges associated with closing the loan. The new policies and procedures do not require the borrower to pay the principal, taxes, and insurance portion of the final payment on the old loan. Only the interest owed to the prior lender will be collected from the borrower, if the amount cannot be financed into the new loan.

Recommendations

We recommend the Assistant Secretary for Housing- Federal Housing Commissioner

1A. Require New Freedom reimburse borrowers for the principal, taxes, and insurance that were inappropriately collected and not applied to the old or new loans. The amount for the 598 loans reviewed is $156,998.

1B. Verify that New Freedom has properly reimbursed the borrowers.

1C. Perform a review of New Freedom to verify that it has implemented its new policies and procedures for collecting payments from borrowers at closing.

1D. Consider referring New Freedom to the Office of RESPA and Interstate Land Sales for review.

SCOPE AND METHODOLOGY

Our audit generally covered the period of March 1, 2002 through February 29, 2004. However, where applicable, the audit period was expanded to include current data through May 14, 2004. We conducted our fieldwork from May through June 2004.

During our audit, we performed tests for compliance with HUD's requirements for the refinancing of Federal Housing Administration-insured loans. Initially we focused on those loans that were refinanced in the State of Utah by New Freedom with beginning amortization dates within our audit period. Based on the initial methodology, we reviewed a sample of 16 federally insured streamline-refinanced loans that had defaulted within the first 12 months of refinancing. During our audit, we expanded our focus to include streamline-refinanced loans processed by New Freedom's main office in Salt Lake City, UT. Those loans included loans from other States. Based on the results of our initial testing, New Freedom performed its own testing. This testing consisted of auditing 796 of the 21,185 streamline refinanced loans processed by the Salt Lake City office, during the period March 1, 2002, to March 31, 2004. We performed additional testing to verify New Freedom's methodology and to determine whether its results were reasonable. We determined that its testing was reasonable; therefore, we relied on New Freedom's results. Additionally, we interviewed a sample of six borrowers in the Denver Metropolitan area who had loans refinanced through the Salt Lake City office and paid the additional monthly mortgage payment on their prior loan at closing. Our sampling methodology was appropriate to obtain an understanding of the borrower's knowledge of the refinancing process.

To determine whether New Freedom acted in a prudent manner and complied with the Act and HUD related requirements in the streamline refinancing of its federally insured loans selected for review and in implementing its Quality Control Plan, we

- Interviewed HUD's management and staff to obtain background information on New Freedom. We gathered information from HUD's Quality Assurance Division and the Denver Homeownership Center concerning New Freedom's business operations.

- Reviewed applicable Federal and HUD regulations, and other applicable reference materials related to single-family requirements.

- Reviewed the Federal Housing Administration case binders and New Freedom's scanned loan case files for our initial 16 sample loans.

- Reviewed and analyzed New Freedom's audit of 796 streamline-refinanced loans to determine if their analysis was valid.

- Reviewed New Freedom's scanned loan case files for the sample of six borrowers selected to interview.

- Performed an analysis of New Freedom's accounting records for the financial transactions recorded on the HUD-1 Settlement Statements for the 16 initial sample loans.

- Interviewed New Freedom officials and staff to obtain information regarding its policies and procedures.

- Interviewed six Denver Metropolitan area mortgagors to determine their understanding of New Freedom's streamline refinancing procedures and costs.

- Reviewed New Freedom's Quality Control Plan and selected a sample of the most recent quality control reviews performed.

- Reviewed the Independent Auditor's Reports for fiscal years 2002 and 2003.

- Relied, in part, on data maintained by HUD in the Single Family Data Warehouse, Neighborhood Watch, and Single Family Insurance System. We did not perform a detailed analysis of the reliability of these systems. However, we did perform testing for the data related to our finding results.

The HUD Office of Inspector General, Denver Office of Audit, worked closely with the Office of RESPA and Interstate Land Sales on the applicable sections of the Act pertaining to our audit.

We performed our review in accordance with generally accepted government auditing standards, which included tests of internal controls that we considered necessary due to our audit objectives.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

- Effectiveness and efficiency of operations;
- Reliability of financial reporting; and
- Compliance with applicable laws and regulations.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives; the processes and procedures for planning, organizing, directing and controlling program operations; and the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objectives:

- Process for streamline refinancing of Federal Housing Administration-insured loans and
- Policies and procedures implemented in the quality control process.

We assessed the relevant controls identified above.

A significant weakness exists if internal controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weakness

Based on our review, we believe the following item is a significant weakness:

- New Freedom collected an inappropriate monthly mortgage payment from borrowers of streamline-refinanced Federal Housing Administration-insured loans; contrary to both the Act and HUD related requirements.

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS PUT TO BETTER USE

Recommendation Number	Unreasonable or Unnecessary 1/
1A	**$156,998**

1/ Unnecessary or unreasonable costs are those costs not generally recognized as ordinary, prudent, relevant, and or necessary within established practices. Unreasonable costs exceed the costs that would be incurred by a prudent person in conducting a competitive business.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Auditee Comments

New Freedom™ MORTGAGE CORP

LEGAL DEPARTMENT
2363 South Foothill Drive
Salt Lake City, Utah 84109

Phone: (801) 493-2744
Fax: (801) 493-2743

September 20, 2004

By FedEx Overnight Mail, and E-mail:
FSmith@hudoig.gov, RGwin@hudoig.com, EKite@oig.gov, and SPon@hudoig.gov

Frederick M. Smith, Senior Auditor
Robert C. Gwin, Regional Inspector General for Audit
Office of Inspector General for Audit, Region 8
Dept. of Housing and Urban Development
UMB Plaza, 1670 Broadway, 24th Floor
Denver, CO 80202-4801

Re: Draft Audit Report for New Freedom Mortgage Corporation

Dear Mr. Gwin and Mr. Smith:

Enclosed with this letter is a corrected, replacement copy of the Auditee's Comments on behalf of New Freedom Mortgage Corporation. It contains technical corrections.

We originally sent the Auditee's Comments to you on Friday, September 17. There were two corrections in wording which had been made (pages 4 and 5), but, for some reason, the changes did not make it to the final draft. Please discard the draft sent to you on Friday, and use this one.

We apologize for any inconvenience this may have caused.

Sincerely,

NEW FREEDOM MORTGAGE CORPORATION

Robert M. Taylor, Esq.
General Counsel

Enclosures
092004 Smith.wpd

Auditee Comments

Introduction.

The Audit Report ("Report") focuses upon a post-dated check which was delivered at closing by numerous borrowers in the Streamline Refinance Program. The check was credited on the HUD-1 Settlement Statement as a "payment". The Report concludes that New Freedom may have inappropriately collected a monthly mortgage payment from the borrowers. Then, on the basis that it was a monthly mortgage payment, it is assumed that New Freedom actually collected principal, interest, taxes and insurance. The Report concludes that all borrowers believed that they were making a payment on their existing loan; concludes that New Freedom did not accurately disclose all costs associated with the loans; and implies that there was a hidden charge or unearned fee.

New Freedom respectfully suggests that this is a matter of misunderstanding, by the examiners, of both the documentation provided to the consumer and the actual application of payments made by the borrowers. New Freedom submits that the facts can only be determined on a case-by-case basis, that the manner and application of payments by the borrowers were not inappropriate, and that the loan costs were all properly disclosed.

The loans were made as part of a marketing plan to enable participation in the Streamline Refinance Program by borrowers who could not qualify to roll in or otherwise afford to pay their accrued interest and closing costs. New Freedom's plan let the borrowers refinance with the same out-of-pocket costs as if they were not refinancing.

Background.

New Freedom has always been a proud supporter and promoter of the FHA Streamline Refinance Program. It has tried and in fact succeeded to facilitate the United States' public policy of encouraging refinances by FHA borrowers, to help those borrowers realize substantial savings in their monthly payments as well as interest over the life of the loans; and to do so in conformance with the HUD guidelines.

While promoting the "no cost" refinances permitted by HUD's guidelines, New Freedom realized that there was a segment of the marketplace which could not qualify to roll in escrows and interest, and could not afford to participate in the Streamline Refinance Program, simply because of the cost of closing. Utilizing the tools made available by the guidelines, New Freedom developed a marketing plan to allow thousands more to enjoy the Streamline Refinance Program, without increasing their mortgage balance in most cases, and to thereby lower their rates and payments. The plan did not call for high fees, nor for loans at above market rates. Loans would be done at relatively small profit margins. The program was designed to enable those who could not qualify to, or did not want to roll accrued interest and closing costs into the refinanced loan, to instead bring a post-dated check to closing in an amount for which they had already budgeted (not to exceed the amount of their existing loan payment). The borrowers would incur no "out-of-pocket" costs; that is, they would be able to refinance without making a payment any greater than the one they had already budgeted for and which would have otherwise been due.

With high volume, New Freedom could implement the plan. New Freedom took the risk that this concept would appeal to low income people, and spent millions of dollars promoting the program. It hired and trained loan officers and underwriters specifically for the program.

To implement the plan, New Freedom's loan officers and underwriters would have to work in each case to find the particular loan structure which would work for the borrower. New Freedom could not describe, in its marketing materials, an exact loan which would work for everyone. So, it tried to describe the conceptual plan in as broad but accurate terms as possible for marketing materials. When someone would call, the loan officers would gather information, consider the various alternatives, and discuss with the borrower what New Freedom could do. There are numerous circumstances which would need to be considered. The application for each borrower would be different. Whatever the circumstance, New Freedom would make its best efforts, within the HUD regulations and guidelines, to help the borrower find a way to make a refinance without paying out more than they would have paid had they not done the refinance.

In this manner, New Freedom believed that it was providing a service which was consistent with public policy, and to the borrowers' advantage. *In fact*, the auditors were apparently impressed with and have acknowledged in the Report that New Freedom's intent and belief was consistent with that goal.

Not a Mortgage Payment. The payment under scrutiny was not a "monthly mortgage payment". It was not "collected" for the prior lender. A post-dated (to the 15th of the following month) check was written to New Freedom. On the HUD-1 Settlement Statement (the "HUD-1") for every one of the applicable audited files, it was called, for example, "October payment". In no case was the post-dated check called "October mortgage payment". The HUD-1 entry was simply intended as a description for an <u>amount</u>, in connection with the marketed concept of no out-of-pocket costs[1].

The Report's finding was that the check was an "inappropriate collection of borrowers' monthly mortgage payment on prior loan". New Freedom Mortgage acknowledges that, when viewed by themselves in the abstract, a combination of phrases in some of the marketing materials and the HUD-1 Settlement Statement might lead one to conclude that New Freedom was collecting a monthly mortgage payment[2]. However, when considered in context with the oral communications and the developments relative to a particular loan, it would be or should be clear to a borrower that the post-dated check payable to New Freedom was not a payment on the prior loan, but rather the borrower's payment at closing; and that it was simply in an amount equal to (or in some cases less than) the prior loan payment, which was geared to fit within their budget, consistent with a program offered by New Freedom.

---

[1] New Freedom tried to use words on the HUD-1 which would connect the post-dated check to the marketing plan. Of course, space is limited on a HUD-1. In the space provided, New Freedom tried to say something which would be meaningful to the borrower. It was intended to bring to mind the borrower's budget, and thereby the no "out-of-pocket" cost concept.

[2] The materials called "Supplemental Closing Instructions for our Borrowers" were, obviously, intended by New Freedom to convey a concept. That document was not sent to all borrowers. Out of context the words might indicate that the whole amount, rather than the interest, would go to the prior lender. That was not the intent. Clearly, not all of the check would go to reimburse money paid to the prior lender. There is no way to know if borrowers relied on those words, rather than the HUD-1 or what they had been told. It is notable that very few of the files in the audit sample contain signed Supplemental Closing Instructions to Borrowers. Based upon the sample reviewed by the auditors, it would appear that perhaps three out of twenty signed those documents. How many of them relied on the wording, rather than any oral communications, could only be determined by an actual empirical study.

The description did not say that it was a "mortgage payment". So, to conclude that New Freedom "collected" principal, taxes and insurance premiums is unfair. Rather, the description simply made reference to the next calendar month (in which the check would be dated, and budgeted), in an effort to connect to the concept which would have been explained in the application and underwriting process. The borrowers understood because of those explanations.

Even apart from those oral communications, New Freedom believes that it would be unfair to conclude that, across the board, borrowers thought that it was a *mortgage* payment. The borrowers would look to the HUD-1, and would see a *credit* recorded for their payment in the 200 section. (A mortgage payment would be a charge.) That credit, combined with other sources of funds, would cover the costs, charges and loan payoff described in the 100 section (and detailed on the second page of the HUD-1).

New Freedom established a program which was to the borrowers' advantage. The words on the HUD-1 were used to simply communicate that the payment was the implementation of the no "out-of-pocket" concept. Whether (and if so, why) a borrower thought it was a mortgage payment, and that principal and/or taxes were being paid thereby, is subject to the factors, circumstances and communications in that borrower's case[3]. It cannot be determined solely from a theoretical analysis based on forms.

Disclosures. The Report suggests that New Freedom failed to disclose how the payment would be applied. The focus, again, is on the words used. The HUD-1 is designed to provide disclosures of all amounts paid in connection with (in this case) a mortgage loan closing. The space provided on the HUD-1 for any particular entry is limited. For each of the loans in the audit sample, the amounts paid out were all disclosed, in the same detail as is traditionally provided. The loan payoff, establishment of an escrow, lender charges and closing costs are all identified in appropriate places. The post-dated checks were referred to as "payments", and identified by the month in which the check would be dated. The HUD-1 affords no room to itemize its specific application. By necessity, a general description was required. As indicated above, the description used was meaningful to the parties involved in the particular transaction. All amounts paid were disclosed, and the post-dated check would serve as a credit for the borrowers' contribution toward them. The rest would be covered by New Freedom.

The description on the HUD-1, e.g. "October payment", was not a reference to wording found in flyers and other marketing materials. Those materials were marketing tools, designed to describe and offer a loan origination service, not a standardized product. The materials do not apply to a particular loan. During the course of the loan application process, each borrower would have received a personalized explanation regarding their loan and the post-dated check. It is therefore unfair to refer to the marketing materials, especially the flyers and other standard materials, to determine what was disclosed to the borrowers in the particular case.

It is important to note that even the marketing materials varied from case to case. New Freedom did not generally advertise "no closing cost to you" (as was suggested in the Report). Rather, in most

[3] It is acknowledged that the Audit Report refers to interviews of six borrowers in Colorado. How they were chosen, and what they were asked is not reported. Nor is there an indication as to which marketing materials they may have received. It is respectfully submitted that it would be extremely difficult, after the fact, to draw a reliable, credible response from borrowers. Their memories would likely have faded, for example, and rather than to make an effort to recall, most would now be likely to be led by the questions, instead. Further, the incentive to give an answer which might lead to a refund is obvious.

cases, it advertised: "no out-of-pocket cost to you". [The "no closing cost to you" flyers were for a different situation. When borrowers qualify to roll in their closing costs, lenders like New Freedom are able to make a streamline refinance without closing costs paid by the borrower at closing. New Freedom did release some flyers for the no closing costs program. It also created and more often used flyers to focus on the out-of-pocket costs, as described above, for the plan which had broader appeal and worked for more people[4].] Because the options available to a particular borrower in a streamline refinance are numerous, the flyers and other materials were written to make reference to a marketing concept; they are not nor could they ever be disclosures applicable to particular borrowers. Each borrower's facts would be analyzed, and each would be advised of what they were qualified to do. Each would make his or her choices. The actual disclosures relative to each particular loan were made in the course of oral communications, and by the actual HUD-1 Settlement Statements at closing, as required by FHA.

No Hidden Charges or Unearned Fees. Consistent with the foregoing, New Freedom respectfully disagrees with the suggestion in the Report that its practices resulted in some way in a hidden charge or unearned fee[5]. All charges and fees associated with the streamline refinanced loans were fully disclosed, and earned. Those costs and charges were summarized in the 100 section of the HUD-1, and detailed on the second page. None were left out.

The HUD-1's show that New Freedom advanced – for the borrower – (a) the loan payoff including all accrued interest, and (b) the closing costs charged by third parties. As is evident by reference to Appendix D, the post-dated check covered the accrued interest on the prior loan, and only part of the closing costs paid to third parties. Please see New Freedom's Appendix D(i). Based upon Appendix D to the Report, Appendix D(i) shows that New Freedom paid $43,266.32 to third parties in connection with the 39 loans audited by the OIG. Yet, after credit for accrued interest the borrowers on those loans reimbursed only $10,238.92 in post-dated checks to New Freedom. In other words, New Freedom received less than one-fourth of those advanced costs back in reimbursement from the borrower. There was no extra money. It did not receive a hidden charge or fee.

New Freedom fully disclosed all charges, costs and fees associated with each loan. A review of the HUD-1 would reveal all of the amounts paid in connection with the refinance, and the borrowers' contribution to those amounts. *The borrowers received full credit for the check delivered, consistent with the purpose for the 200 section of the HUD-1.* The HUD-1 would also reveal the lender's contribution to those amounts. The borrowers' contribution was less than the amount New Freedom paid out for the borrowers. New Freedom did not inappropriately receive the money. It paid out more than it got back.

Comments Re: Recommendations From the Report.

New Freedom engaged in a marketing plan, in good faith, with the desire to deliver the benefits of the Streamline Refinance Program to people who might not have been able to participate otherwise, because of the cost involved in closing a loan. New Freedom engaged in the plan at its own significant

---

4 In March, 2003, a Quality Assurance Division of HUD in Philadelphia, Pennsylvania, reviewed and approved a flyer with the "no out-of pocket costs to you" message.

5 The Report implies that the post-dated check was really a hidden charge or an unearned fee. Excerpts from the law are even attached, in Appendix C. A close review reveals law prohibiting hidden charges and unearned fees; but nothing which relates to the circumstances addressed in the Report. Furthermore, even if the HUD-1 was completed inaccurately, we note that RESPA does not provide for a penalty for failure to properly fill in a HUD-1 Settlement Statement, especially if done inadvertently.

expense and substantial risk. In fact, by accepting post-dated checks from the borrowers, it took and in many cases realized the down side risk that those checks would not be collected. Furthermore, due to early defaults, New Freedom had to repay investors any monies which they made. The repayments totaled $5,677.81 on the loans listed on Appendix D, for example. (Certainly, it would be patently unfair to reimburse or pay money to the borrowers in those categories.)

If some of the borrowers misunderstood, and truly thought that another payment was due to their previous lender, and further believed that they had no obligation to contribute to the costs of closing, at all, and if those facts could be objectively and reliably determined, then some remedial action would be appropriate. New Freedom would reimburse those borrowers. However, it would not be fair to require New Freedom to do so for all borrowers who wrote a post-dated check to New Freedom. Each case is different. Each loan is different. Each borrower's experience in the process must be evaluated on a case-by-case basis. New Freedom made full disclosure, and the borrowers were given the information, and understood, or should have, that the post-dated check was their only out-of-pocket contribution. It was fair and consistent with the plan that they would pay only the amount and at the time they were accustomed to paying on their old mortgage.

This is a technical issue. New Freedom could, admittedly in 20/20 hindsight, have found other wording in its marketing materials and on the HUD-1. Nonetheless, the wording was meaningful to each individual borrower in the context of their individual loan. It is important to note that FHA has conducted 6 different audits during the audit period. In each case they reviewed refinance files like these. Not once was it suggested that there might be a problem.

This is not an issue of harm. To the contrary, each borrower received, without "out-of-pocket" expense, what they wanted: a refinanced loan, at a lower interest rate, and a lower payment (or shorter term) on fair and competitive terms. In the sample which is the subject of the report, the borrowers reduced their rate by an average of 1.573%. In that sample, the borrowers reduced their monthly payments by an average of $63.54. Furthermore, and perhaps most significantly, the borrowers will save a total (life of loan) of $26,706.81 on average, for a total of $1,041,565.50. (See Appendix D(i).)

New Freedom provided a service which was intended to be, and in the result was, tailored to the borrowers' individual circumstances. Each borrower received a real benefit. No clear violation has been demonstrated, and no harm has been suffered. Rather, the charges are based on misunderstanding of the wording on the HUD-1, and a suggestion that some unrelated marketing materials might be read to imply a meaning that was not intended by New Freedom. The loans were refinanced through an individualized process, and, so, to apply that suggestion across the board would not be consistent with the facts. It would therefore be unfair to require New Freedom to reimburse or repay money to everyone who has a loan containing the questioned wording. Such a payment would unjustly enrich the borrowers – who have not been harmed – and unjustly punish New Freedom.

Nonetheless, New Freedom is sensitive to the concerns of the auditors, and would be pleased to make prospective adjustments to its materials, procedures and practices, without prejudice to any of the allegations in the Audit Report. New Freedom would welcome thoughts and comments from the HUD program staff.

Submitted September 20, 2004

New Freedom Mortgage Appendix D(i)

	Case #	Pmt Collected at closing	Int Amount	Excess collected per IG Audit	Lender Credit for Closing Costs	Actual 3rd Party Closing Costs	Loan #	Borrower	Closed	Loan Amt	Monthly Savings	Life of Loan Savings	Term Reduction in months
1	023-1949663-734	$ 495.60	$ 428.86	$ 66.74	$ 874.54	$ 809.45	190531	BOYLES	12/19/2003	$ 72,650.00	$ 83.10	$ 29,916.00	0
2	045-6201949-703	$ 823.00	$ 557.36	$ 265.64	$ 1,060.94	$ 1,123.05	169719	TEA	12/17/2003	$ 84,124.00	$ 39.90	$ 9,576.00	120
3	052-2667177-703	$ 841.00	$ 620.47	$ 220.53	$ 1,071.43	$ 1,042.73	125370	TROYER	2/18/2003	$ 99,791.00	$ 125.88	$ 45,316.80	0
4	052-2667618-703	$ 940.00	$ 683.13	$ 256.87	$ 1,161.40	$ 978.45	126955	SHOWELL	2/21/2003	$ 118,339.00	$ 80.72	$ 29,059.20	0
5	052-2767937-734	$ 664.00	$ 478.61	$ 185.39	$ 864.22	$ 945.45	137771	GOLDMAN	4/23/2003	$ 82,533.00	$ 54.71	$ 19,695.60	0
6	052-2904423	$ 1,343.00	$ 1,021.35	$ 321.65	$ 1,123.32	$ 1,021.45	154217	GORDY	6/18/2003	$ 161,981.00	$ 169.14	$ 60,890.40	0
7	052-3049463-703	$ 864.40	$ 578.84	$ 285.56	$ 520.03	$ 1,113.45	166767	HILL	8/21/2003	$ 94,370.00	$ 98.10	$ 35,316.00	0
8	052-3075463-703	$ 1,221.00	$ 765.85	$ 455.15	$ 1,775.16	$ 1,114.45	175248	HOWELL	9/15/2003	$ 138,182.00	$ 128.76	$ 46,353.60	0
9	092-9638061-703	$ 718.00	$ 468.17	$ 249.83	$ 1,063.86	$ 1,665.35	188114	LORD	12/23/2003	$ 80,999.00	$ 42.19	$ 13,922.70	30
10	093-5686211-703	$ 815.18	$ 412.72	$ 402.46	$ 1,070.65	$ 1,798.19	186084	FARRELL	12/18/2003	$ 67,618.00		$ -	180
11	093-5701653-703	$ 597.00	$ 423.61	$ 173.39	$ 776.92	$ 1,138.45	190024	ASHURST	12/22/2003	$ 61,136.00	$ 120.50	$ 43,380.00	0
12	105-1696759-703	$ 534.62	$ 395.21	$ 139.41	$ 956.55	$ 1,421.19	194196	PRUITT JR	12/19/2003	$ 68,032.00	$ 43.84	$ 15,782.40	0
13	137-2123511-734	$ 569.28	$ 492.64	$ 76.64	$ 995.69	$ 1,242.45	190199	SONNE	12/22/2003	$ 83,395.00	$ 69.62	$ 25,063.20	0
14	412-5134240-703	$ 695.00	$ 478.95	$ 216.05	$ 1,611.26	$ 1,099.45	189293	MCCARTY	12/22/2003	$ 72,267.00	$ 109.68	$ 39,484.80	0
15	431-4034498-703	$ 832.00	$ 520.52	$ 311.48	$ 705.66	$ 878.25	189118	MYHRE	12/19/2003	$ 92,707.00	$ 44.79	$ 16,124.40	0
16	441-7405186-703	$ 531.00	$ 330.46	$ 200.54	$ 1,151.56	$ 1,223.20	189557	REEVES	12/19/2003	$ 53,445.00	$ 49.13	$ 17,686.80	0
17	441-7412351-703	$ 740.00	$ 464.36	$ 275.64	$ 1,172.70	$ 1,341.70	191588	TROSTLE	12/23/2003	$ 72,056.00	$ 127.26	$ 45,813.60	0
18	441-7419568-703	$ 537.00	$ 336.28	$ 200.72	$ 1,061.14	$ 1,217.95	193504	ORTIZ	12/18/2003	$ 51,494.00	$ -	$ -	180
19	441-7424320-703	$ 829.00	$ 381.15	$ 447.85	$ 973.68	$ 1,343.20	193171	VANCE	12/18/2003	$ 62,508.00	$ 97.61	$ 35,139.60	0
20	442-2448901-703	$ 570.00	$ 361.73	$ 208.27	$ 1,093.04	$ 1,217.70	190135	STROUD	12/12/2003	$ 57,377.00	$ -	$ -	180
21	442-2451969-703	$ 534.00	$ 326.63	$ 207.37	$ 1,128.64	$ 1,239.20	192182	GALLAGHER	12/22/2003	$ 52,017.00	$ 55.65	$ 20,034.00	0
22	491-8245999-703	$ 626.04	$ 504.31	$ 121.73	$ 1,222.65	$ 1,235.39	189526	KERELUK	12/17/2003	$ 84,169.00	$ -	$ -	180
23	491-8274030-703	$ 747.00	$ 390.20	$ 356.80	$ 1,150.33	$ 877.60	193948	DARGAN	12/22/2003	$ 62,517.00	$ 49.85	$ 17,946.00	0
24	492-7039436-703	$ 1,025.00	$ 461.36	$ 563.64	$ 913.97	$ 1,394.02	190906	ALEXANDER	12/19/2003	$ 82,191.00	$ 74.98	$ 26,992.80	0
25	493-7595611-703	$ 828.00	$ 305.47	$ 522.53	$ 281.18	$ 1,222.85	180572	BARNES	12/18/2003	$ 63,734.00	$ -	$ -	120
26	493-7661546-703	$ 780.00	$ 623.48	$ 156.52	$ 3,603.00	$ 1,060.70	192634	GONZALEZ	12/18/2003	$ 109,721.00	$ 97.66	$ 35,157.60	0
27	493-7674901-703	$ 607.00	$ 349.20	$ 257.80	$ 521.23	$ 942.90	192843	SALINAS	12/22/2003	$ 47,355.00	$ -	$ -	180
28	494-3015430-703	$ 756.00	$ 414.82	$ 341.18	$ 1,490.12	$ 943.19	187316	MARIN, JR	12/18/2003	$ 74,663.00	$ 30.48	$ 10,972.80	0
29	494-3016777-703	$ 560.00	$ 341.65	$ 218.35	$ 694.47	$ 848.44	187975	MEDRANO	12/22/2003	$ 51,356.00	$ 80.47	$ 28,969.20	0
30	495-6600474-703	$ 806.00	$ 502.10	$ 303.90	$ 655.76	$ 794.65	154367	PETRILLI	12/24/2003	$ 87,624.00	$ 9.94	$ 2,982.00	0
31	495-6746816-703	$ 870.00	$ 616.32	$ 253.68	$ 3,204.71	$ 1,191.08	186615	WISSINGER	12/22/2003	$ 104,392.00	$ 76.87	$ 27,673.20	0
32	495-6814026-703	$ 847.00	$ 453.95	$ 393.05	$ 854.43	$ 1,173.58	190587	EATON	12/19/2003	$ 76,336.00	$ 104.56	$ 37,641.60	0
33	521-5067517-703	$ 894.00	$ 706.19	$ 187.81	$ 755.72	$ 779.45	78649	TERRY	2/14/2002	$ 99,219.00	$ 101.40	$ 36,504.00	0
34	521-5493079-703	$ 1,004.00	$ 778.43	$ 225.57	$ 865.18	$ 821.45	132161	COOK	3/17/2003	$ 127,943.00	$ 109.80	$ 39,528.00	0
35	521-5530347-734	$ 1,200.00	$ 858.96	$ 341.04	$ 1,412.47	$ 1,148.45	135743	CRAM	4/23/2003	$ 155,800.00	$ 125.90	$ 45,324.00	0
36	521-5538311-703	$ 1,165.00	$ 896.59	$ 268.41	$ 767.58	$ 912.45	138134	GONZALEZ	4/11/2003	$ 130,800.00	$ -	$ -	180
37	521-5553167-703	$ 766.11	$ 529.03	$ 237.08	$ 885.63	$ 1,025.45	141234	KOTTER	6/23/2003	$ 93,425.00	$ 98.33	$ 35,398.80	0
38	521-5780401-703	$ 571.67	$ 419.13	$ 152.54	$ 815.28	$ 822.45	177194	PAPPAS	9/22/2003	$ 112,569.00	$ 113.39	$ 129,600.00	0
39	541-6940370-703	$ 561.00	$ 390.89	$ 170.11	$ 960.22	$ 1,071.05	193435	ROBINSON	12/17/2003	$ 67,073.00	$ 50.89	$ 18,320.40	0
				$ 10,238.92	$ 43,266.32	$ 43,239.91					$ 1,842.60	$ 1,041,565.50	1350
							Average Savings Rate/Monthly/Life			1.573%	$ 63.54	$ 26,706.81	

OIG Evaluation of Auditee Comments

New Freedom suggests that the finding is a matter of misunderstanding. They further state that the manner and application of borrower's payment was appropriate and the loan costs were fully disclosed. The borrowers were given appropriate information and should have understood that their payment was only their normal out of pocket contribution that equaled, for the most part, their normal mortgage payment. The borrower's contribution was only for the amount the borrower was accustomed to paying monthly on their old mortgage. Therefore, New Freedom concludes there was no harm to the borrower.

As our finding states, we evaluated a sample of streamline-refinanced loans. For each of the loans that contained a borrower's payment, we evaluated the documents and disclosures for each particular case. For each of these cases, there were no disclosures or other documentation to support New Freedom's assertion the borrower's payment was their only out of pocket contribution and was the monthly mortgage amount the borrower was accustomed to paying on their old loan. In fact, as our finding details, the documents that mentioned the payment indicated it was the final payment that would payoff the current loan.

Additionally, the borrowers we interviewed believed the monthly payment was necessary to payoff their current loan. The borrowers further believed their payment was used to reimburse New Freedom's advance of the borrower's last month mortgage payment at closing.

New Freedom collected an inappropriate payment from some borrowers for their streamline-refinanced loans. New Freedom collected these payment to help offset its lender-paid closing costs on its advertised "no closing cost to you' or "no out-of-pocket cost to you" streamline-refinanced loans. As such, New Freedom did not comply with the Act and related HUD requirements.

Appendix C

CRITERIA

Real Estate Settlement Procedures Act (the Act)

The Act contains these statutory provisions:

Section 4 of the Act (12 United States Code 2603) states that the HUD-1 Settlement Statement "shall conspicuously and clearly itemize all charges imposed upon the borrowers and all charges imposed upon the seller in connection with the settlement… The HUD-1 Settlement Statement is a standard form that should clearly show all charges imposed on the borrowers in connection with the settlement.

Section 5 of the Act (12 United States Code 2604) requires that "each lender shall…(give) a good faith estimate of the amount of or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement…"

Section 8 of the Act (12 United States Code 2607) prohibits kickbacks and unearned fees and states, **"**No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed."

HUD Requirements

The following HUD requirements provide further guidance, interpretation, and clarification of the Act criteria.

Appendix A of title 24, part 3500, of the Code of Federal Regulations contains the instructions for completing the HUD-1 Settlement Statement, which is required under Section 4 of the Act. Appendix A further states, "This form is to be used as a statement of actual charges and adjustments to be given to the parties in connection with the settlement." The HUD-1 Settlement Statement is supposed to show the actual settlement costs of the loan transaction. The mortgage company must clearly disclose all fees charged in settlement transactions so that the consumer (i.e., borrower) can understand the nature and recipient of the payments.

Title 24, part 203, section 27, of the Code of Federal Regulations, lists the charges, fees, and discounts that the mortgagee may collect from the mortgagor. It states "Reasonable and customary amounts, but not more than the amount actually paid by the mortgagee" may be charged for such other reasonable and customary charges as may be authorized by the Commissioner. Subsection (d) of this part requires the mortgagee to furnish a signed statement in a form satisfactory to the Secretary of Housing and Urban Development, listing any charges, fees, or discounts collected by the mortgagee from the mortgagor. Additionally, it states that all charges, fees, or discounts are subject to review by the Secretary both before and after endorsement under part 203, section 255. The HUD-1 Settlement Statement is the signed form satisfactory to the Secretary.

The customary and reasonable fees and charges that may be collected from the borrower by the mortgagee are identified in HUD Handbook 4000.2, rev-2, section 5-3. The Handbook states, "The HUD Field Office Manager may authorize or reject any other charge or the amount of any charge based on what is reasonable and customary in the area." Section 5-5 of the Handbook prohibits unearned fees and specifically states, "A mortgagee is not permitted to pay any fee, compensation, or thing of value: 1) Other than for services actually performed."

Additionally, the regulations implementing the Act under title 24, part 3500, section 14 of the Code of Federal Regulations prohibit unearned fees. Part 3500, section 14(c) states, "No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed**.** A charge by a person for which no or nominal services are performed or for which duplicative fees are charged is an unearned fee and violates this section."

Title 24, part 203, section 24, of the Code of Federal Regulations, states that the mortgagee shall apply the monthly payments collected from the mortgagor to the following items in the set out order: (1) premium charges under the contract for insurance, charges for group rents, taxes, special assessments, flood insurance premiums, and fire and other hazard insurance premiums; (2) interest on the mortgage; (3) amortization of the principal of the mortgage; and (4) late charges, if permitted. Additionally, the regulations implementing the Act under title 24, part 3500, section 17 of the Code of Federal Regulations set out the requirements for an escrow account that a lender establishes in connection with a federally related mortgage loan. It sets limits for escrow accounts using calculations based on monthly payments and disbursements within a calendar year. The mortgagee shall use the procedures set forth in part 3500, section 17 of this title, implementing Section 10 of the Act (12 United States Code 2609), to compute the amount of the escrow, the methods of collection and accounting, and the payment of the bills for which the money has been escrowed.

HUD Handbook 4330.1, REV-5, states the requirements for establishing escrow accounts. Section 2-5 states, "Escrow funds shall be used only for the purpose for which they were collected and are subject to audit and examination by HUD."

Appendix D

OVERPAYMENT SPREADSHEET

Number of Loans Reviewed	FHA Case Number	Prior Loan's Mortgage Payment Collected At Closing	Interest Due on Prior Loan	Inappropriate Amount Applied to Lender Paid Closing Costs
1	023-1949663	$495.60	$428.86	$66.74
2	045-6201949	$823.00	$557.36	$265.64
3	052-2667177	$841.00	$620.47	$220.53
4	052-2667618	$940.00	$683.13	$256.87
5	052-2767937	$664.00	$478.61	$185.39
6	052-2904423	$1,343.00	$1,021.35	$321.65
7	052-3049463	$864.40	$578.87	$285.53
8	052-3075463	$1,221.00	$765.85	$455.15
9	092-9638061	$718.00	$468.17	$249.83
10	093-5686211	$815.18	$412.72	$402.46
11	093-5701653	$597.00	$423.61	$173.39
12	105-1699759	$534.62	$395.21	$139.41
13	137-2123511	$569.28	$492.64	$76.64
14	412-5134240	$695.00	$478.95	$216.05
15	431-4034498	$832.00	$520.52	$311.48
16	441-7405186	$531.00	$330.46	$200.54
17	441-7412351	$740.00	$464.36	$275.64
18	441-7419568	$537.00	$336.28	$200.72
19	441-7424320	$829.00	$381.15	$447.85
20	442-2448901	$570.00	$361.73	$208.27
21	448-2451969	$534.00	$326.63	$207.37
22	491-8245999	$626.04	$504.31	$121.73
23	491-8274030	$747.00	$390.20	$356.80
24	492-7039436	$1,025.00	$461.36	$563.64
25	493-7595611	$828.00	$305.47	$522.53
26	493-7661546	$780.00	$623.48	$156.52
27	493-7674901	$607.00	$349.20	$257.80
28	494-3015430	$756.00	$414.82	$341.18
29	494-3016777	$560.00	$341.65	$218.35
30	495-6600474	$806.00	$502.10	$303.90
31	495-6746816	$870.00	$616.32	$253.68
32	495-6814026	$847.00	$453.95	$393.05
33	521-5067517	$894.00	$706.19	$187.81
34	521-5493079	$1,004.00	$778.43	$225.57
35	521-5530347	$1,200.00	$858.96	$341.04
36	521-5538311	$1,165.00	$896.59	$268.41
37	521-5553167	$766.11	$529.03	$237.08
38	521-5780401	$571.67	$419.13	$152.54
39	541-6940370	$561.00	$390.89	$170.11
	Totals:	$30,307.90	$20,068.98	$10,238.92

Average Amount of Inappropriate Principal, Taxes, and Insurance: $262.54